

STATE OF NEW YORK

DIVISION OF TAX APPEALS

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In the Matter of the Petition	:	
of	:	
<b>JOHN MCNAMARA</b>	:	DETERMINATION
		DTA NO. 816990
for Revision of a Determination or for Refund of Tax on	:	
Gains Derived from Certain Real Property Transfers under	:	
Article 31-B of the Tax Law.	:	

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Petitioner, John McNamara, Register #3951-053 Piedmont A, Federal Prison Camp, Seymour Johnson, Call Box 8004, Goldboro, North Carolina 27533-8004, filed a petition for revision of a determination or for refund of real property transfer gains tax under Article 31-B of the Tax Law.<sup>1</sup>

On November 21, 1999, petitioner, by his duly appointed representative, Eugene B. Fischer, Esq., and the Division of Taxation by Barbara G. Billett, Esq. (Herbert M. Friedman, Jr., Esq., of counsel) waived a hearing and agreed to submit the matter for determination based upon documents and briefs to be submitted by March 24, 2000, which date commenced the six-month period for issuance of this determination.<sup>2</sup> After due consideration of the evidence and arguments submitted, Jean Corigliano, Administrative Law Judge, renders the following determination.

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<sup>1</sup>Article 31-B of the Tax Law was repealed by the Legislature in 1996 (L 1996, ch 309, § 171, eff July 13, 1996, applicable to transfers occurring on or after June 15, 1996). Citations to Article 31-B in this determination are to the law in effect at the time the Notice of Determination was issued.

<sup>2</sup>After the expiration of the briefing period, Mr. Friedman and Mr. Fischer submitted letters, each attacking statements made in the other's brief. Inasmuch as the letters add nothing to the resolution of the issues, they are not being considered here.

### ***ISSUES***

I. Whether petitioner's forfeiture of his interest in an entity with an interest in real property under provisions of the Federal code of crimes and criminal procedure (18 USC § 591) was a transfer as defined by Tax Law § 1440(7), and, if so, whether there was consideration for the transfer thus subjecting the transfer to gains tax.

II. Whether the Division of Taxation issued a notice of determination to petitioner after the statutory period for doing so had expired.

III. Whether the audit procedures used by the Division of Taxation lacked a rational basis.

IV. Whether petitioner was denied due process of law as a result of the seizure of books and records by agents of the Federal government and petitioner's concomitant inability to obtain the records of Route 347 Realty Corporation to defend himself in this administrative hearing.

V. Whether petitioner had reasonable cause for failure to file statutorily mandated gains tax returns and to pay the tax required to be shown as due on those returns.

### ***FINDINGS OF FACT***

1. Petitioner, John McNamara, was the sole shareholder and president of Route 347 Realty Corporation ("347 Realty"), a New York corporation. 347 Realty was the sponsor of a 30-unit residential condominium offering plan in Port Jefferson, New York known as The Highlands Condominium IIA ("Highlands").

2. In September 1989, 347 Realty filed an initial Real Property Transfer Gains Tax Transferor Questionnaire in accordance with the provisions of Article 31-B of the Tax Law. 347 Realty reported estimated anticipated gross consideration on the project of \$4,627,709.61, an original purchase price of \$3,865,997.26 and total estimated gain of \$486,743.67. This questionnaire was signed by John McNamara. At the same time, 347 Realty filed a Schedule of

Original Purchase Price showing actual amounts expended as of the date of the filing and estimated amounts through completion of the project.

3. On May 17, 1991, 347 Realty filed a project update revising the amounts reported in the 1989 filing. As pertinent here, petitioner reported the following:

	Actual to Date	Total Anticipated
Anticipated gross consideration	\$ 2,367,898.56	\$ 4,453,591.56
Brokerage Fees	103,548.84	226,451.04
Anticipated consideration	2,264,349.72	4,227,140.52
Purchase Price to Acquire	270,000.00	270,000.00
Other acquisition costs	4,714.68	4,714.68
Cost of capital improvements	1,757,925.77	3,400,762.07
Conversion costs	26,484.41	30,667.23
Original purchase price	2,059,124.86	3,706,143.98
Gain subject to tax	(205,224.86)	520,996.54

4. 347 Realty filed three Tentative Assessment and Return forms (form TP-582) with the Division reporting the sale of three condominium units.<sup>3</sup> The first form TP-582 was filed on March 1, 1990 and reported the transfer of unit 104 and a tax due of \$1,582.89. The second form TP-582 was filed on July 23, 1990 and reported the transfer of unit 99 and a tax due of \$1,936.27. The third form was filed on May 14, 1992 and reported the transfer of unit 30 with a tax due of \$2,237.29. Petitioner signed these forms, as well as the original transferor questionnaire and first project update, as president of 347 Realty.

5. In May 1992, the assets of 347 Realty, including the Highlands, were placed under the power of a special trustee appointed by Judge Edward R. Korman of the United States District Court of the Eastern District of New York. The appointment resulted from a criminal investigation of fraud and corruption conducted by the United States Department of Justice.

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<sup>3</sup> This is not to suggest that no other forms TP-582 were filed by 347 Realty. According to the audit report, 347 Realty paid gains tax of \$27,296.00 prior to 1994 which exceeds the total amount of tax shown as due on the three forms submitted by the Division. However, only three forms TP-582 were placed in the record.

Petitioner was accused, and eventually convicted, of criminal fraud and racketeering in connection with a scheme of false loan applications perpetrated against General Motors Acceptance Corporation. By the time his conduct was discovered, he had obtained over a billion dollars in fraudulent loans. Petitioner also admitted bribing local officials to get approval for his real estate projects and developments. In August 1996, petitioner was sentenced to five years in a Federal prison and ordered to repay the \$412 million he still owed General Motors.

6. A Decree of Forfeiture and Order Appointing a Special Trustee (the “Decree”) was filed in Federal district court on May 18, 1992 pursuant to the civil forfeiture provisions of the Federal code of crimes and criminal procedure (18 USC § 591). The plaintiff in the action is the United States of America (“USA”). Various corporations owned or controlled by petitioner are the named defendants *in rem*, including 347 Realty. Certain real property and premises located at 133 Main Street, Port Jefferson, New York and 142 Main Street, Port Jefferson, New York are also named as defendants in the action. It does not appear from the documents in the record that the Highlands was included in these two parcels of real property. Petitioner is not a named defendant. The first paragraph of the Decree provides as follows:

1. Pursuant to USC § 981, any interest of John McNamara, direct or indirect, personally or through entities he controls, in all assets of the defendants *in rem* including, without limitation, all properties, books, records, hardware, software (including computer programs, data bases, tapes, disks and all other media), promissory notes, cash, bonds, securities, security instruments, furniture, fixtures, accounts receivable, real property, personal property and other assets, of whatever nature and wherever located shall be forfeited to the United States of America.

7. The Decree appoints a “Special Trustee of the defendants *in rem*” (“Special Trustee”), and the defendants *in rem* were deemed to be in the custody of the Special Trustee as agent for

the Attorney General. All actions and proceedings concerning the defendants *in rem* were stayed pending order of the court.

8. Paragraph 5 of the Decree provides as follows:

Any and all receivers, custodians, trustees or similar persons heretofore appointed with respect to the defendants *in rem* hereby are directed to (a) immediately turn over to the Special Trustee the defendants *in rem* together with any and all rents, profits and issue derived from the defendant Assets, (b) disclose to the Special Trustee the nature, amount and location of any and all defendant assets, (c) take such actions as may be requested by the Special Trustee which are necessary to affect a transfer of dominion and control of any defendant to the Special Trustee, and (d) refrain from the payment of any real property tax, personal property tax, income tax or other similar tax relating to the defendants pending further Order of this Court.

9. The powers of the Special Trustee were stated in paragraph 6 of the Decree. As relevant here, the Special Trustee was authorized to administer and manage the daily affairs of the defendants *in rem* and to take general administrative actions with respect to the management, conservation and liquidation of the defendants *in rem*; to obtain and maintain possession of all bank deposits, broker or investment accounts, safe deposit boxes or other accounts belonging to any of the defendants *in rem*; to determine, classify and record all claims of any persons or entities claiming an interest in the defendants *in rem* and the basis and amount of the claims; to provide notice of the Decree and Order to all potential claimants; to negotiate with claimants or restructure any claim to the defendants *in rem*; to arrange for the sale, liquidation or other disposition of the defendants *in rem* in a commercially reasonable manner; to deposit the proceeds of sale or liquidation into the Asset Forfeiture Fund administered by the United States Justice Department ("Forfeiture Fund"); to apply to the court for an order directing payment of all approved claims from the Forfeiture Fund; to supervise and dismiss all employees or

managers of the defendants *in rem*. The powers delegated to the Special Trustee in other relevant provisions of paragraph 6 are as follows:

j. enter into contracts, leases or other agreements, and incur and pay debts and expenses on behalf of the defendants;

k. take possession of, administer, invest, sell, dispose and conserve the defendants *in rem*;

l. hire, appoint, retain and discharge legal counsel, accountants, investigators, officials, experts, consultants, employees and/or advisors (collectively, the "Retained Professionals") to perform his administrative and operational functions and otherwise to assist the Special Trustee in performance of the responsibilities set forth herein;

o. take possession of and review all current and past books, records, files, accounts and correspondence of the defendants;

p. to the extent and in the manner directed by the U.S. Attorney's Office, seek recovery to the extent permitted by law, of any assets dissipated or otherwise misappropriated by the owners of the defendants *in rem*, and pursue all causes of action, equitable or legal, and claims possessed by the owners of the defendants *in rem*.

10. Interim reports filed with Judge Korman by the Special Trustee indicate that real property owned by 347 Realty was sold and transferred by the Special Trustee, but there is no mention of the Highlands in the reports placed in evidence or any indication that any individual condominium units in the Highlands were sold by the Special Trustee.

11. The Division conducted an audit of 347 Realty which was completed sometime between December 1994 and May 1995.<sup>4</sup> It is not known when the audit was commenced or what efforts were made to obtain information regarding the transfer of the Highlands condominium units.

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<sup>4</sup> The audit report contained workpapers but no narrative description of how the audit was conducted. A memorandum dated December 12, 1994 contains the final computation of tax due, but other workpapers are dated May 16, 1995.

12. The Division concluded that 12 units were sold between January 1, 1990 and January 1, 1991 including units 114 and 99 (for which gains tax returns were submitted into the record). The Division determined that gains tax of \$27,296.00 was paid, presumably in connection with the transfer of 12 units through January 1991. The remaining 18 units were treated as unsold, including unit 30 which was one of the three units for which there is evidence of a gains tax return having been filed and tax paid.<sup>5</sup> Actual prices were obtained for the 12 units which were sold in 1990, and from these the Division calculated gross consideration received of \$1,807,287.00. Consideration for the 18 unsold units was estimated based upon prices listed in the Highlands offering plan. Gross consideration for these units was determined to be \$2,758,820.00. Thus, gross consideration for the entire plan was determined to be \$4,566,107.00. This amount was reduced by brokerage fees of \$103,549.00 yielding net consideration of \$4,462,558.00. The Division used the May 17, 1991 project update summarized in Finding of Fact “3” to estimate original purchase price. Acquisition costs (including the purchase price of the property, taxes, insurance and legal fees) were accepted as reported. The Division reduced the reported conversion costs and costs of capital improvements by 50% “due to lack of substantiation.” This resulted in total original purchase price of \$1,990,430.00 and anticipated gain of \$2,472,128.00 with a tax liability of \$247,213.00. This amount was reduced by previous payments of \$27,296.00, resulting in tax due of \$219,917.00 plus penalty and interest. Interest was calculated from July 15, 1991 indicating that the Division treated the May 17, 1991 project update as a final return.

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<sup>5</sup> The Division issued a Conciliation Order, dated November 20, 1998, which states that payments of \$2,426.89 have been applied to the statutory notice in issue; presumably, this payment is related to the transfer of unit 30.

13. On July 7, 1995, the Division issued to petitioner a Notice of Determination of gains tax due in the amount of \$219,917.00 plus interest of \$83,730.47 and penalty of \$21,991.00 for a total due of \$325,638.47. The notice states: “This notice is issued because you are liable as an Officer/Responsible Person [of 347 Realty Corporation] for taxes determined to be due in accordance with sections 1440, 1444(c) and 1447.3(a) of the New York Tax Law.”

14. Letters written by the Special Trustee to Judge Korman show that the assets of 347 Realty were under the control of the Special Trustee and that many of those assets were sold by the Special Trustee. However, there is no mention in these letters of the Highlands condominium units.

15. Petitioner’s attorney attempted to obtain access to the records of the Special Trustee but was informed that the records were unavailable.

16. In an affirmation, J. Timothy Shea, petitioner’s attorney in connection with the sales of individual Highlands condominium units, established that, for each sale made by 374 Realty prior to the forfeiture, a tentative assessment and return was prepared, signed by petitioner and filed along with the gains tax due for that transaction.

#### ***SUMMARY OF THE PARTIES’ POSITIONS***

17. Petitioner argues that he is not liable for the gains tax assessed by the Notice of Determination. He makes the following arguments:

(a) The Notice of Determination was issued after the expiration of the three-year period of limitation for assessment of additional gains tax which petitioner measures from the date of the last gains tax filing in the record, May 13, 1991.

(b) The Decree did not result in a transfer of real property that would require the filing of a gains tax return under Article 31-B of the Tax Law. The government took control of the



corporate entity, 347 Realty, and, through it, possession of the Highlands; therefore, 347 Realty remained the owner of the real property, before and after the filing of the Decree. Even if this is deemed to be a transfer for gains tax purposes, there was no consideration for the transfer, and, therefore, no transaction taxable under Article 31-B.

(c) The audit of 347 was arbitrary and unreasonable, and the Notice of Determination lacks a rational basis.

(d) Petitioner was denied due process of law as a result of his inability to obtain any records of 347 Realty after the forfeiture.

(e) Petitioner had reasonable cause for failure to file returns or pay tax when due since all records of 347 Realty were seized by the Federal government and petitioner was denied access to those records.

18. The Division responds to petitioner's arguments as follows:

(a) The statutory period of limitation was not triggered because a final questionnaire was never filed; therefore, the Division was authorized by Tax Law § 1444(3)(a) to issue a determination of tax due at any time.

(b) Petitioner was a person liable for tax pursuant to Tax Law § 1440(8) and (9);

(c) As a result of the Decree, there was a taxable transfer of real property by 347 Realty in May 1992 which the Division describes as follows:

Tax Law former section 1440(7) defines the "transfer of real property" as ". . . the transfer of any interest in real property by any method . . ." . *See also*, 20 NYCRR former section 590.4. The Petitioner concedes that his interest in Route 347 (which was the "controlling interest" as discussed, *supra*) was obtained by the USA. Further, the evidence shows that Route 347's interest in the Project was

forfeited to the USA by the Forfeiture Order of May 18, 1992. Plainly, the USA's seizure constitutes a "transfer" for gains tax purposes.<sup>6</sup>

The Division argues that the consideration for this transfer was relief from debts owed by petitioner when the Special Trustee sold property owned by 347 Realty and paid claimants with the proceeds.

(d) The Division was authorized by Tax Law § 1444(1) to make a determination of tax due based on the information available to it, and, in light of the paucity of information available, the Division's audit was reasonable.

(e) Petitioner has received notice of the tax due, the basis for the determination and an opportunity to be heard satisfying the requirements of due process.

(f) Penalties are appropriate because petitioner failed to file a final update questionnaire and tentative assessment upon transfer of the interest in Highlands to the USA, and he has not shown that he had reasonable cause not to make such a filing.

### ***CONCLUSIONS OF LAW***

A. Tax Law § 1441(1) imposes a 10 percent tax on "gains derived from the transfer of real property within the state." Gain is defined in Tax Law § 1440(3) as "the difference between the consideration for the transfer of real property and the original purchase price of such property, where the consideration exceeds the original purchase price." The "[t]ransfer of real property" means:

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<sup>6</sup> Neither the Notice of Determination nor the audit report refer to the transfer of an interest in a controlling entity; furthermore, the audit report calculates gain based on a 100% sell out of all units as of May 1991, and interest is calculated from July 1991. It is not apparent from this that the forfeiture was a triggering event which resulted in the issuance of the Notice of Determination or that the tax was calculated based upon a controlling entity transfer. However, since this is the only theory of taxation articulated by the Division, it is the only basis for the imposition of tax that will be addressed in this determination.

the transfer of any interest in real property by any method including, but not limited to sale, exchange, assignment, surrender, mortgage foreclosure, transfer in lieu of foreclosure, option, trust indenture, taking by eminent domain, conveyance upon liquidation or by a receiver, or transfer or acquisition of a controlling interest in any entity with an interest in real property. (Tax Law § 1440[7]).

I agree with the Division that this definition of a “transfer” is broad enough to encompass petitioner’s forfeiture of his interest in 347 Realty to USA. By that forfeiture, USA acquired a 100 percent interest in 347 Realty which was an entity with an interest in real property (*see, Matter of Martinez*, Tax Appeals Tribunal, October 16, 1997). Therefore, a transfer of real property occurred for purposes of section 1440(7). However, I agree with petitioner that there was no consideration for the transfer; therefore, there was no gain at the time of the transfer. Since there was no gain, the transfer was not subject to gains tax.

B. Consideration means the “price paid or required to be paid for real property or any interest therein” including the cancellation or discharge of an indebtedness or of an obligation (Tax Law § 1440[1][a]). Consideration is fixed at the moment of transfer and is not affected by subsequent events (*see, Matter of Starburst Development*, Tax Appeals Tribunal, May 5, 1994). The moment of transfer in this case was the forfeiture of petitioner’s interest in 347 Realty to USA on May 18, 1992 pursuant to the Decree. To calculate consideration for the transfer, the transaction must be viewed from the perspective of the transferee, in this case USA, and the question to be asked is what price was paid or required to be paid by the transferee for the interest in real property (*see, Matter of Ziegelman*, Tax Appeals Tribunal, October 12, 1995). The answer is nothing. USA gave no consideration to petitioner for his interest in 347 Realty, and petitioner received nothing of value.

It is the nature of a forfeiture that one gives up all rights and interests in the forfeited property and receives nothing in exchange. USA incurred no obligations as a result of the

forfeiture. None of petitioner's debts or obligations were cancelled; no lien was released; no mortgage was satisfied; no claim against him, criminal or civil, was dropped. No obligation of 347 Realty was satisfied as a result of the transfer. The only claims which could be made under the Decree were claims against the assets of the defendants *in rem*, including 347 Realty. However, the forfeiture did not directly provide for the settlement of any claims against 347 Realty that might have existed at the time of the forfeiture. The Special Trustee was authorized to administer and manage the daily affairs of 347 Realty and to sell or liquidate the assets of 347 Realty. Any income realized as a result of the Special Trustee's administration was to be deposited in the Forfeiture Fund. Those monies could then be drawn on to pay claims against the assets of the defendants *in rem*. There is nothing in the Decree that indicates that liquidation of the assets of 347 Realty would necessarily be applied to the debts of 347 Realty. Petitioner is not a defendant in the forfeiture Decree, he could make no claims against the defendants *in rem* and he had no interest or claim to any of the proceeds which resulted from sales or liquidation of the assets of 347 Realty. In short, no consideration was paid or required to be paid by USA to petitioner for the transfer of his interest in 347 Realty. Petitioner simply forfeited his interest in 347 Realty to the government.

347 Realty continued to hold real property and to operate under the custody of the Special Trustee after the forfeiture. The Special Trustee had the authority to sell real property owned by 347 Realty in the normal course of business. Whether it did so or not is not known and also is not relevant to the question of whether there was consideration given for the forfeiture, since the consideration was fixed at the time of the forfeiture and could not be increased or decreased by subsequent events (*Matter of Starburst Development, supra*). The facts that can be ascertained

from the record establish that the forfeiture was not a transfer subject to gains tax and that petitioner had no claims against USA or 347 Realty after the forfeiture.

C. In view of the conclusions reached above, the other issues raised by the parties need not be addressed.

D. The petition of John McNamara is granted, and the Notice of Determination, dated July 7, 1995 is cancelled.

DATED: Troy, New York  
June 29, 2000

/s/ Jean Corigliano  
ADMINISTRATIVE LAW JUDGE